

**AGENDA ITEM: Fiscal Year 2019 Audit Documents**

**Background**

Arizona Administrative Code R7-5-504(A) requires that by July 1 of each year, the Board make available on its website written requirements regarding the audit each charter school is required to submit annually under A.R.S. §§ 15-183(E)(6) and 15-914. Pursuant to Board rule, the written requirements (also referred to as the audit documents) for fiscal year 2019 must be released by July 1, 2019. The audit documents include the audit guidelines, Legal Compliance Questionnaire, Uniform System of Financial Records for Charter Schools (USFRCS) Compliance Questionnaire, and Procurement Compliance Questionnaire.<sup>1</sup>

**Proposed Changes to Audit Documents**

Audit Guidelines

The proposed revisions to the audit guidelines may be found in Appendix A and include making clarifying and technical changes (e.g., updating years and dates).

Legal and USFRCS Compliance Questionnaires

First, Board staff is proposing the following changes to the Legal and USFRCS Compliance Questionnaires to reflect current requirements or statutory language.

	Reason for Change	FY18 Language	Proposed FY19 Language
<p><b>“Required Filings” section, Part 1c (Legal)</b></p> <p><b>“Financial Reporting” section, Part 10c (USFRCS)</b></p>	Update statutory reference	“Arizona Department of Economic Security <b>A.R.S. §23-721 et seq.</b> ”	“Arizona Department of Economic Security <b>A.R.S. §§23-701 through 23-757</b> ”
<p><b>“Required Filings” section, Question 4 (Legal)</b></p> <p><b>“Budgets” section, Question 6 (USFRCS)</b></p>	Remove question as it only applied to fiscal year 2018	“Did the school maintain records to support the number of eligible teachers, eligible teachers’ salaries, and employer share of retirement expense to appropriately calculate and distribute the 1.06% teacher salary increase? ( <b>Laws 2017, Chapter 305, §33</b> )”	<i>Question eliminated</i>
<p><b>“Classroom Site Fund” section, Question 4 (Legal and USFRCS)</b></p>	Update language to align with current statute	“For Project 1013, were expenses only for class size reduction, teacher compensation increases, AIMS intervention programs, teacher development, dropout prevention programs, and teacher liability insurance premiums?”	“For Project 1013, were expenses only for class size reduction, teacher compensation increases, <u>assessment</u> intervention programs, teacher development, dropout prevention programs, and teacher liability insurance premiums?”

Second, [A.R.S. § 15-914\(G\)](#) gives the Office of the Auditor General (OAG) the responsibility to establish a method to audit average daily membership. On April 16, 2019, the OAG notified Board staff that changes will

<sup>1</sup> The fiscal year 2018 audit documents may be accessed at <https://asbcs.az.gov/school-resources/additional-resources/annual-audits>.

be made to the student attendance reporting questions and that proposed changes have been provided to the Arizona Department of Education (ADE) for review and comment. The OAG anticipates having the changes to the student attendance reporting questions finalized by May 15, 2019. As of the writing of this report, the nature of the changes is not known. The Board has historically incorporated in its Legal Compliance Questionnaire and USFRCS Compliance Questionnaire changes made by the OAG under A.R.S. § 15-914(G).

Finally, the OAG notified Board staff that it would be updating the questionnaire the OAG issues for charters sponsored by universities to include a question asking if the charter submitted its Classroom Site [Fund] Project Narrative Summary (narrative summary) to ADE. A.R.S. § 15-977(J) requires charters and school districts to submit the narrative summary for the fiscal year that ended on June 30 by November 15 of each year. Board staff has not incorporated this question in the changes proposed above for the following reasons:

1. In addition to being the deadline for submitting the narrative summary to ADE, November 15 is the deadline for Board-sponsored charters to submit their financial statement audits to the Board. Currently, between 75 and 80 percent of the more than 400 audits submitted annually to the Board are due by November 15. Since the deadline for submitting the narrative summary and the financial statement audit are the same, in many cases, this question would likely either be answered “N/A” or be answered based on the prior year’s narrative summary submission. Therefore, adding this question to the Board’s questionnaires would not provide useful or current information to the Board.
2. Beginning with fiscal year 2018, Board staff requested and received from ADE a list of charters that had not yet submitted the fiscal year 2018 narrative summary. Similar to the process used for the Annual Financial Reports (or AFRs), Board staff followed up with the charters that had not submitted the narrative summary. Board staff plans to continue this process in subsequent years. Further, failure to submit the narrative summaries will be noted on the charter holder’s operational performance dashboard and may result in the charter holder being placed on a Board agenda for possible disciplinary action.

#### Procurement Compliance Questionnaire

[A.R.S. § 15-213\(F\)](#) gives the OAG the responsibility to establish a method to audit schools’ compliance with procurement practices. On April 16, 2019, the OAG notified Board staff that changes will be made to the procurement questions. The OAG anticipates having these changes finalized and issued by May 15, 2019. As of the writing of this report, the nature of the changes is not known. The Board has historically incorporated in its Procurement Compliance Questionnaire changes made by the OAG under A.R.S. § 15-213(F).

#### **Requested Board Action**

Since the Board does not plan to meet in June, Board staff is asking the Board today:

- To approve the fiscal year 2019 audit guidelines and changes identified above to the Legal Compliance Questionnaire and USFRCS Compliance Questionnaire.
- To direct Board staff to incorporate the OAG and ADE student attendance reporting and procurement changes available by June 24, 2019 into the Board’s Legal Compliance Questionnaire, USFRCS Compliance Questionnaire and Procurement Compliance Questionnaire.
- To date all audit documents based on the date the documents will be released, which must be no later than July 1, 2019.

## **APPENDIX A**

### **PROPOSED FY19 AUDIT GUIDELINES**

## Arizona State Board for Charter Schools

### Physical Address

1616 W. Adams St., Suite 170  
Phoenix, AZ 85007



### Mailing Address

P.O. Box 18328  
Phoenix, AZ 85005

**TO :** Administrators of charter schools sponsored by the State Board for Charter Schools

**FROM :** Andrea Leder, Assistant Director of Operations & Finance

**DATE :** ~~June 29, 2018~~XXXX

**SUBJECT :** Audit Guidelines

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Arizona Revised Statutes (A.R.S.) §§ 15-183(E)(6) and 15-914 require all charter schools to have an annual audit. Pursuant to A.R.S. § 15-914, charter school audits must be conducted in accordance with *Government Auditing Standards*. This memorandum is designed to provide general guidance to you and your audit firm on charter school audit requirements and applies only to audits of charter schools sponsored by the Arizona State Board for Charter Schools (Board).

### Mandatory Audit Firm Qualifications

The following qualifications are mandatory for audit firms that wish to conduct charter school audits:

1. The auditors must be properly licensed certified public accountants or persons working for a licensed certified public accounting firm according to *Government Auditing Standards* (GAS).
2. The audit firm must meet the independence requirements of GAS.
3. The audit firm must have an external peer review performed at least every 3 years in accordance with GAS. The most recent external peer review report must be provided to the charter holder and the Board.
4. The audit firm must meet the continuing education requirements of GAS. Therefore, each auditor responsible for planning, directing, conducting, or reporting on GAS audits should complete at least 80 hours of continuing education every 2 years. At least 20 hours should be completed in any 1 year of the 2-year period. At least 24 of the 80 hours of continuing education should be completed in subjects directly related to the government environment, government auditing, or the specific or unique environment in which the charter school operates. The audit firm does not need to provide the Board with evidence that continuing education requirements have been met. However, the audit firm will be required to include a statement in the engagement letter affirming that the audit firm meets all of the mandatory qualifications set forth in this section. (For more information, please see the "Engagement Letter Approval" section.)

5. In accordance with Arizona Administrative Code (A.A.C.) R7-5-504(B), the audit firm and supervising certified public accountant must not be subject to a current or pending disciplinary action or a regulatory action requiring the audit firm or supervising certified public accountant to complete conditions specified by an accounting industry regulatory body. An audit firm's or supervising certified public accountant's status with the Arizona Board of Accountancy may be ascertained at <http://www.azaccountancy.gov/CPADirectory/CPASearch.aspx>.

### **Audit Type**

***Single Audit*** – Charter holders organized as governmental and not-for-profit entities that expend \$750,000 or more in federal awards are subject to the requirements of the *Single Audit Act Amendments of 1996* and Title 2 U.S. Code of Federal Regulations (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance), and are required to obtain an annual single audit. The audit requirements imposed by the *Single Audit Act Amendments of 1996* referenced in this memorandum apply specifically to organizations that are the primary reporting entity. In cases where the school is not the primary reporting entity – i.e., the school is part of a larger organization or considered a subsidiary of another organization that holds the charter – these requirements apply only to the primary reporting entity and not the school. However, sufficient test work must be conducted at the school level to complete the applicable compliance questionnaire(s) in accordance with both the agreed upon procedures (instructions contained therein) and the attestation standards established by the American Institute of Certified Public Accountants (see below for more information on the compliance questionnaires). If the school is the only part of the primary reporting entity that received federal financial assistance, the entity may choose to apply these requirements just to charter school operations.

***Financial Statement Audit*** – Charter holders not subject to the *Single Audit Act Amendments of 1996* must contract for at least an annual financial statement audit pursuant to A.R.S. § 15-914. In cases where the school is not the primary reporting entity – i.e., the school is part of a larger organization or considered a subsidiary of another organization that holds the charter – the audit may be of the larger organization. However, sufficient test work must be conducted at the school level to complete the applicable compliance questionnaire(s) in accordance with both the agreed upon procedures (instructions contained therein) and the attestation standards established by the American Institute of Certified Public Accountants (see below for more information on the compliance questionnaires). The reporting entity may also choose to apply these requirements just to the charter school operations.

All audits, regardless of type, must be based on the state's fiscal year of July 1 through June 30.

### **Compliance Questionnaires**

In addition to the financial statement or single audit, the audit firm must complete the appropriate compliance questionnaire(s) in accordance with both the agreed upon procedures (instructions contained therein) and the attestation standards established by the American Institute of Certified Public Accountants. All Board sponsored charter holders should obtain the applicable compliance questionnaire(s) from the Board's website (<https://asbcs.az.gov/school-resources/additional-resources/annual-audits>) and not the Auditor General's website. Each charter holder is responsible for providing a copy of the appropriate compliance questionnaire(s) to the audit firm contracted to perform the audit. To determine which compliance questionnaire(s) must be completed, please see below:

- USFRCS Compliance Questionnaire – **This questionnaire is applicable only to charter holders that are subject to the Uniform System of Financial Records for Charter Schools (USFRCS).** The current USFRCS Compliance Questionnaire is dated ~~6/18/XX~~ and must be used for all fiscal year 2018-2019 audits.
- Legal Compliance Questionnaire – **This questionnaire is applicable to charter holders that have received an exception to the USFRCS.** It is used by Board staff to determine if a charter holder is complying with certain legal requirements. The current Legal Compliance Questionnaire is dated ~~6/18/XX~~ and must be used for all fiscal year 2018-2019 audits.
- Procurement Compliance Questionnaire – **This questionnaire is applicable to charter holders that have NOT received an exception from procurement rules** and should be completed in conjunction with either the USFRCS Compliance Questionnaire or the Legal Compliance Questionnaire. The current Procurement Compliance Questionnaire is dated ~~6/18/XX~~ and must be used for all fiscal year 2018-2019 audits.

The applicable compliance questionnaire(s) must be completed in accordance with both the agreed upon procedures (instructions contained therein) and the attestation standards established by the American Institute of Certified Public Accountants for each charter contract the charter holder has with the Board. For example, if the charter holder has three separate charter contracts with the Board and has received exceptions to the USFRCS and procurement rules for all three, then a Legal Compliance Questionnaire must be completed and submitted for each charter contract. Please note that multiple compliance questionnaires would not be required if the charter holder operated three sites under one charter contract. Under this scenario, assuming the charter holder has received USFRCS and procurement exceptions, one Legal Compliance Questionnaire must be completed and submitted. In completing the one Legal Compliance Questionnaire, the audit testing and question responses would incorporate all three sites.

### **Engagement Letter Approval**

Laws 1999, 1<sup>st</sup> S.S., Ch. 4, sec. 15 requires the Board to approve the audit contract prior to audit commencement. The Board uses the engagement letter to meet this requirement. At this time, the Board is only approving one-year engagement terms. A copy of the engagement letter must be submitted to the Board for approval before any audit work begins. The Board prefers that engagement letters be submitted by email to [Audits@asbcs.az.gov](mailto:Audits@asbcs.az.gov). Please note that faxed engagement letters are not accepted. Engagement letters must be on the firm's letterhead. **Engagement letters received by the Board that are not on firm letterhead will be returned and not processed.**

The following items must be included in the engagement letter for the Board to consider its approval:

1. Review of Audit Guidelines – The engagement letter must reference that either the audit firm has reviewed the Board's audit guidelines dated ~~June 29, 2018 XXXX~~ or that the audit services to be provided meet the Board's audit guidelines dated ~~June 29, 2018 XXXX~~.
2. "Mandatory Audit Firm Qualifications" Affirmation – The engagement letter must include a statement affirming that the audit firm meets all of the mandatory qualifications set forth in the "Mandatory Audit Firm Qualifications" section (see Page 1).
3. Government Auditing Standards (GAS) – Since A.R.S. § 15-914 requires all charter school audits be conducted in accordance with GAS, all engagement letter must state that the audit

will be conducted in accordance with these standards and that the audit will include the report required by GAS.

4. Compliance Questionnaire(s) – The engagement letter must include a statement indicating that the audit firm will complete the appropriate compliance questionnaire(s) as required by the Board in accordance with both the agreed upon procedures (instructions contained therein) and the attestation standards established by the American Institute of Certified Public Accountants.
5. Specific Fee Information – The engagement letter must include specific fee information. If the engagement letter is for a single audit, includes fees for other services, or both, the engagement letter should specify the fee by service [e.g., \$X for the financial statement audit and completion of the appropriate compliance questionnaires(s), \$Y for the single audit, \$Z for the preparation of the information return].
6. Retention and Availability of Audit Documentation – Minimally, the engagement letter must include the following or similar language related to the retention and availability of the audit documentation:

“The audit documentation for this engagement is the property of [name of audit firm] and constitutes confidential information. However, pursuant to the authority given by law or regulation, we may be requested to make certain audit documentation available to your sponsor or its designee for purposes of reviewing the audit’s quality, resolving audit findings, or carrying out oversight responsibilities. If requested, access to such audit documentation will be provided under the supervision of [name of audit firm]. Furthermore, upon request, we may provide photocopies of selected audit documentation to your sponsor or produce the audit documentation at your sponsor’s office. Your sponsor may intend, or decide, to distribute the copies or information contained therein to others, including other governmental agencies. All audit documentation will be retained in its entirety for a period of 5 years after the report release date unless your sponsor requests a longer retention period.”

The Board will disapprove any engagement letter that fails to address the requirements specified in this section or in A.A.C. R7-5-504(B).

Please note that by approving the engagement letter, the Board is not giving any assurance that the audit fee requested is reasonable, the projected completion date will be attained, or the audit reporting package will comply with applicable auditing standards and the minimum audit and reporting standards prescribed by the Board.

#### **Complete Audit Reporting Packages**

The audit firm shall provide at least one copy of the complete audit reporting package to the charter holder, one copy to the Board by email to [Audits@asbcs.az.gov](mailto:Audits@asbcs.az.gov) (see “Audit Deadline/Timeframe” section), and one copy to the Arizona Department of Education Grants Management by email to [grants@azed.gov](mailto:grants@azed.gov).

For single audits, the audit firm shall also provide one copy of the audit reporting package and data collection form to the Federal Audit Clearinghouse’s Internet Data Entry System at the following address: <https://harvester.census.gov/facweb/>.

For an audit reporting package to be considered complete, it must include at least the following:

For Financial Statement Audits:

1. Financial statements, including the audit firm's opinion thereon
2. *Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards*
3. The applicable compliance questionnaire(s) as described above with an agreed upon procedures report thereon in accordance with the attestation standards established by the American Institute of Certified Public Accountants
4. Management letter issued, if applicable

For Single Audits:

In addition to the items listed above for financial statement audits:

1. Schedule of Expenditures of Federal Awards, including the audit firm's report thereon
2. Report on Compliance for Each Major Federal Program and Report on Internal Control Over Compliance Required by the Uniform Guidance
3. Summary Schedule of Prior Audit Findings
4. Schedule of Findings and Questioned Costs
5. Corrective Action Plan

In accordance with A.A.C. R7-5-504(E), a charter holder that fails to submit timely a complete audit reporting package may be subject to charter oversight as specified in A.A.C. R7-5-601 and following.

**Audit Deadline/Timeframe**

The deadline to submit the complete audit reporting package to the Board is November 15<sup>th</sup>, except that an extension is possible only for a charter holder that is subject to the *Single Audit Act Amendments of 1996*. The Board has not authorized staff to grant extensions for other reasons. In order to consider granting a single audit extension, the Board must receive an engagement letter for a single audit from the charter holder or its audit firm by November 15<sup>th</sup> and prior to the commencement of the audit. Single audit extensions are only granted through the engagement letter process.

The complete financial statement audit reporting package may either be sent electronically to [Audits@asbcs.az.gov](mailto:Audits@asbcs.az.gov) **or** mailed to the Board at P.O. Box 18328, Phoenix, AZ 85005 **or** delivered to the Board's office at 1616 W. Adams Street, Suite 170 in Phoenix. The Board prefers that financial statement audit reporting packages be submitted by email. Complete financial statement audit reporting packages received by the Board on or before November 15<sup>th</sup> by 11:59 p.m. for emailed copies or by 5 p.m. for paper copies will be considered timely submitted. Please note that faxed financial statement audit reporting packages are not accepted. Financial statement audit reporting packages must be on the firm's letterhead and include the appropriate signatures. Financial statement audit reporting packages received by the Board that are not on firm letterhead and/or do not contain



the appropriate signatures will be returned and not processed. For those choosing to submit a paper copy of the financial statement audit reporting package, the Board will accept an unbound and double-sided copy.

For charter holders that receive a single audit extension, a complete single audit reporting package must be submitted by March 31<sup>st</sup>. The Board prefers that single audit reporting packages be submitted by email to [Audits@asbcs.az.gov](mailto:Audits@asbcs.az.gov). ~~Since March 31, 2019 falls on a Sunday, e~~Complete single audit reporting packages received by the Board on or before ~~Monday, April 1, 2018~~ March 31<sup>st</sup> by 11:59 p.m. for emailed copies or by 5 p.m. for paper copies will be considered timely submitted. Please note that faxed single audit reporting packages are not accepted. Single audit reporting packages must be on the firm's letterhead and include the appropriate signatures. Single audit reporting packages received by the Board that are not on firm letterhead and/or do not contain the appropriate signatures will be returned and not processed. For those choosing to submit a paper copy of the single audit reporting package, the Board will accept an unbound and double-sided copy.

**Failure to submit a complete financial statement or single audit reporting package by the specified deadline will be noted on the charter holder's operational performance dashboard and may result in the charter holder being placed on the next Board meeting agenda for possible disciplinary action.**

#### **Review of Complete Audit Reporting Packages**

The annual audit reporting package serves as one of the primary tools used by the Board to carry out its statutorily mandated oversight responsibilities for the charter schools it sponsors. As such, each audit reporting package is reviewed in accordance with A.A.C. R7-5-504(F)-(H) and the Board's [Audit & Compliance Questionnaire Follow-up Matrix](#).

Additionally, Laws 1999, 1<sup>st</sup> S.S., Ch. 4, sec. 15 requires the Board to approve the completed audit reporting packages. In accordance with this statutory requirement, if, as part of Board staff's review conducted pursuant to A.A.C. R7-5-504(F)-(I), possible issues are identified (e.g., issues related to the accuracy of information in the audit reporting package), Board staff will follow-up with the charter holder, audit firm, or both as described in the "Review of Audit Firm Performance/Adherence to Standards" section below. Please note that the review of the audit reporting package conducted pursuant to A.A.C. R7-5-504(F)-(I) is not the same as the completeness determination made in accordance with A.A.C. R7-5-504(C)-(D) and addressed in the "Complete Audit Reporting Packages" section beginning on Page 4.

#### **Review of Audit Firm Performance/Adherence to Standards**

In accordance with Laws 1999, 1<sup>st</sup> S.S., Ch. 4, sec. 15, the Board reviews the audit reporting packages and may review audit documentation of audit firms performing charter school audits to determine the quality of technical performance and adherence to the cited standards and to determine whether the audit firms met the minimum standards prescribed by the Board for completing the compliance questionnaires.

To that end, if as part of Board's staff review conducted pursuant to A.A.C. R7-5-504(F)-(I), possible issues are identified, Board staff will follow-up with the audit firm, charter holder, or both as follows:

- For possible issues related to the financial statements and related disclosures (e.g., the accuracy of this information), Board staff will first contact the audit firm to discuss the possible issue and, if an issue indeed exists, determine if it involves an oversight or mistake by the audit firm. If an oversight or mistake occurred, the audit firm will be asked to correct

the issue and submit revised financial statements or related disclosures, as applicable, to the Board and the charter holder. If an issue does exist, but does not involve an oversight or mistake by the audit firm, Board staff will contact the charter holder as the entity responsible for the financial statements to discuss the identified issue. If the issue or combination of issues is determined to be significant enough, the charter holder may be asked to reissue the financial statements.

- For possible issues related to the GAS report or the compliance questionnaires (e.g., the completeness or accuracy of this information), Board staff will contact the audit firm to discuss the possible issue and, if an issue indeed exists, will ask the audit firm to correct the issue and submit the revised document(s) to the Board and to the charter holder. If the audit firm fails to correct the issue, Board staff will send a letter to the audit firm's client, asking for the charter holder's assistance. If Board staff's review identifies that the audit firm did not complete the compliance questionnaire(s) in accordance with the prescribed minimum audit standards (e.g., all "No" and "N/A" answers are not adequately explained), Board staff will notify both the audit firm and charter holder and will provide a deadline by which the audit firm must submit the revised questionnaire(s) to the Board and the charter holder.

Based on issues identified through the review of complete audit reporting packages or to help ensure that the minimum standards prescribed by the Board in its compliance questionnaires are being adhered to, Board staff may ask to review certain documentation or require the audit firm to produce the documentation at the Board's office in a format that is accessible by the Board. The documentation shall be subject, at all reasonable times, to review upon request by the Board. Board staff will coordinate any such requests with the audit firm.

#### **Adjustment for Audit Costs**

Schools that are only required to have an annual financial statement audit may be reimbursed for audit costs paid from state and local monies by increasing their budgets, as outlined in A.R.S. §15-914(F). Specific instructions for calculating this increase have been included in the charter school annual budget forms and budget work sheets. These worksheets are available at <http://www.azauditor.gov/reports-publications/charter-schools/manuals-memorandums>. The Arizona Department of Education receives copies of the engagement letters approved by the Board and uses them when determining the audit cost adjustment.

Schools that are required to have a single audit may charge audit costs applicable to each federal program to the appropriate federal project. This action requires filing a project amendment with the Arizona Department of Education and budgeting an appropriate amount under Support Services—Business, function code 2500, and Purchased Professional and Technical Services, object code 6300. Any remaining audit costs, however, should be paid for from state and local monies.

#### **Questions**

If you have any questions or need assistance, please contact Andrea Leder at (602) 364-3106 or [Andrea.Leder@asbcs.az.gov](mailto:Andrea.Leder@asbcs.az.gov).